ANUARUL AINI MOHD. PERAI & ANOR.

v.

KETUA PENGARAH KASTAM & EKSAIS DIRAJA MALAYSIA, JOHOR BAHRU

HIGH COURT MALAYA, JOHOR BAHRU
JAMES FOONG JC
[ORIGINATING SUMMONS NO. 24-327 OF 1989]
19 NOVEMBER 1990

CUSTOMS AND EXCISE: *Sales tax - Licensed manufacturer - Debenture - Fixed charge - Receivers appointed - Monies due to Customs Office - Whether sales tax ranks in priority to fixed charge - Whether federal tax - Administrative duties of Receivers - Whether civil debt owed to government - Preferential treatment - Date of occurrence of sales tax - Date debt due to debenture holders - Whether immovable properties - Sales Tax Act 1972, s. 70 - Government Proceedings Act 1956, s. 10.*

REVENUE LAW: *Sales tax - Debenture - Receivers - Priority - Whether debt to government - Sales Tax Act 1972, s. 70 - Government Proceedings Act 1956, s. 10.*

S, a licensed manufacturer under the Sales Tax Act 1972 (the 1972 Act), issued a debenture in the form of a first fixed charge over certain assets in favour of MIDF. The plaintiffs were appointed Receivers by MIDF and sold S's fixed assets for RM1.2 million. The defendants claim a sum of RM55,226.52 from the plaintiffs alleged to be due by S to the defendants under s. 70 of the 1972 Act.

The issue for the Court is whether taking into account s. 70 of the 1972 Act, sales tax ranks as a priority payment over a fixed charge of a debenture holder in the event where Receivers are appointed.

Held:

[1] (a) The position in this case is not similar to both ss. 191 or 292 of the Companies Act since this is not a case of a floating charge or a case involving winding-up of the company.

(b) Apart from ss. 191 and 292 there are no statutory provisions under the Companies Act or elsewhere which provide guidelines to Receivers appointed under a fixed charge.

[2] The sales tax in the case falls within the confines of federal tax.

[3] Section 70 of the 1972 Act standing on its own does not provide a priority payment for sales tax so incurred; it merely sets out the duties of the Receiver which are administrative duties and administrative duties cannot be taken to infer priority payments.

[4] This Court adopted the view of Starke J in the *Farley's* case where it stated that the setting aside of money sufficient to provide for taxation is only an administrative function; however it does not confer priority rights over other claims.

[5] As sales tax is a civil debt as defined by s. 23 of the 1972 Act then s. 10 of the Government Proceedings Act applies.

[6] (a) From the affidavits before this Court, the sales tax in this case were incurred before the appointment of the Receivers.

(b) The debt due to the debenture holders can be taken as the date of appointment of the Receivers; therefore this debt was due after the sales tax was incurred.

[7] (a) The assets secured are in fact movable properties and therefore do not qualify under the exception of s. 10(2) of the Government Proceedings Act 1956.

[8] Sales Tax being a debt owed to the Government ranks in priority over fixed charge of debenture holders.

[Order accordingly.]

Cases referred to:
Re Golden Palace Musical Hall Sdn. Bhd. [1988] 2 MLJ 634
Federal Commissioner of Taxation v. Official Liquidator of E. O. Farley Ltd. [1940] 63 CLR 278

Legislation referred to:
Companies Act 1965, ss. 191, 292
Government Proceedings Act 1956, s. 10, (2)
Sales Tax Act 1972, ss. 23, 70, (1)

For the Plaintiffs - Abraham & Partners
For the Defendants - Idrus bin Harun (Penasihat Undang-Undang Kastam dan Eksais DiRaja Malaysia)

JUDGMENT

James Foong JC:

The plaintiffs in this case are the Receivers appointed by a financial institution known as Malaysian Industrial Development Finance Bhd. (MIDF) under debenture issued by a company known as Setama Sdn. Bhd. (Setama) in favour of MIDF.

Under the said debenture a first fixed charge over certain assets (hereinafter referred to as the fixed assets) of Setama as set out in the fourth schedule of the debenture was created in favour of MIDF.

When the Receivers were appointed on 11 August 1988, they gave notice of their appointments to the Director General of Custom and Excise of Malaysia (the defendants in this case) as required under s. 70(1) of the Sales Tax Act 1972. This notice was given for reason that Setama is a licensed manufacturer as defined under the Sales Tax Act.

In carrying out their duties as Receivers, the Receivers took possession of the fixed assets of Setama and caused them to be sold for RM1.2 million.

The loan under the debenture due by Setama to MIDF stood at RM1,760,196.89. Therefore even with the recovery from the proceeds of sale it is insufficient to repay in full to MIDF the outstanding loan due by Setama.

The Receivers received a letter from defendants stating that there is an outstanding sum of RM55,226.52 due by Setama to the defendants under the Sales Tax Act and that the Receivers should pay over this sum to the defendants. The defendants' claim is based on s. 70 of the Sales Tax Act.

The Receivers by way of originating summons apply to this Court for directions seeking *inter alia* a declaration that the Receivers are not liable to pay the said sum of RM55,226.52 due as sales tax and excise duties to the defendants in priority to the fixed charge created under the said debenture in favour of MIDF.

The whole issue of this case arises from the wording of s. 70 of the Sales Tax Act.

Section 70 is divided into 3 sub-sections and these are reproduced below:

> 70(1) Where a receiver is appointed of the property of a licensed manufacturer the receiver shall give notice thereof to the Director General within fourteen days thereafter, and shall before disposing of any of the assets of the licensed manufacturer set aside such sum out of the assets as appears to the Director General to be sufficient to provide for any sales tax that will thereafter become payable in respect of the goods that have been sold or manufactured by the licensed manufacturer before the appointment of the receiver.
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> (2) A person appointed as receiver who fails to give notice to the Director General within the time specified in subsection (1) or fails to provide for payment of the sales tax as required by that sub-section shall be personally liable for any sales tax that is or becomes payable as aforesaid.
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> (3) Where two or more persons are appointed receivers the obligations and liabilities attaching to a receiver under this section shall attach to all such persons jointly and severally, subject to a right of contribution between themselves as in cases of contract.

It is argued by the Receivers that s. 70(1) of the Sales Tax Act does not have provisions relating to payment of the sum required to be set aside before disposing of the assets of Setama. Section 70(1) only requires the setting aside of such sum and as no provisions for payment is stated therein, sales tax levied in this case does not become a priority in payment over and above debenture holders of a fixed charge.

The defendants on the other hand interpret s. 70 of the Sales Tax Act to provide a priority in payment over the debenture holders of a fixed charge. The defendants' reason is mainly based on the fact that since s. 70(1) expressly provides for the setting aside of a sum sufficient for the payment, it should follow that such payment would be classified as preferential payment when it comes to distribution in the case of this nature.

The issue before this Court is whether sales tax ranks as a priority payment over fixed charge of a debenture holder in the event where Receivers are appointed.

This Court was invited to refer to two sections of the Companies Act. The two sections referred to are s. 191 and s. 292 of the Companies Act.

Section 191 of the Companies Act provides direction for distribution to receiver appointed under debenture secured by a **floating charge**. Under s. 191 the receiver is required to make preferential payment first before the debenture holders receive their dues. Such preferential payments are mainly wages, salary, vacation leave or superannuation or provident fund of employees of a company under receivership. Federal taxes are not listed as a preferential payment under s. 191.

Section 292 of the Companies Act on the other hand provides direction on distribution to liquidator where a company is under winding-up proceedings.

Under s. 292 the liquidator has to pay six categories of preferential payments before secured creditors receive their dues. Similarly the preferential payments are mainly payments due to employees. However, the last category, ranking 6th in line of preferential payments is federal taxes. Therefore federal taxes take priority before secured creditors in the event of a company being wound up.

However, as noted the position in this case is not similar to both s. 191 or s. 292 of the Companies Act since this is not a case of a floating charge or a case involving winding-up of the company.

Besides s. 191 and s. 292 of the Companies Act, there are no statutory provisions under the Companies Act or elsewhere which provide guidelines to Receivers appointed under a fixed charge.

The defendants brought to the attention of this Court the decision of Mr. Justice Peh Swee Chin in *Re Golden Palace Musical Hall Sdn. Bhd*. [1988] 2 MLJ 634 wherein the circumstances of that case is almost similar to that of this case except in that case the tax involved was service tax. The relevant provisions of Service Tax Act 1975 are identical to the Sales Tax Act.

In *Re Golden Palace* the learned Judge decided that the service tax being a federal tax takes priority over principal and interest of debenture holders.

As regards to the type of tax, I find that the sales tax in this case falls within the confines of federal tax.

After requesting for further submissions from both Counsels, the defendants forwarded to this Court fresh grounds namely the connection of this case to Government Proceedings Act 1956, Act 359.

Section 10 of the Government Proceedings Act 1956 states as follows:

> Section 10(1) All debts due and claims owing from time to time by any person to the Government, whether upon judgment, bond, or other specialty or upon simple contract or otherwise, shall be entitled from the date of the accrual thereof, respectively, to a preference of payment over all debts or claims of every kind which shall, subsequent to such date, have been contracted or incurred by or become due from such person to any other person whomsoever.
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> (2) Nothing herein contained shall affect any right vested in any person by virtue of a mortgage or charge of immovable property duly registered in the manner provided by law for the registration of such mortgage or charge.

After careful consideration of the facts and the authorities so submitted, this Court is of the view that sales tax has a preference of payment over debenture holders of fixed charge in this case.

Section 70 of the Sales Tax Act standing on its own does not provide a priority payment for sales tax so incurred.

Section 70 merely sets out the duties of the receiver which are mainly as follows:

(1) notification of the receiver's appointment to the Director General,

(2) setting aside such sums as appear to be sufficient to the Director General before a sale of the assets of the company under receivership and

(3) in the event that the aforesaid are not done, then the receiver shall be personally liable to any such tax that is or becomes payable.

The duties stated above are administrative duties and administrative duties cannot be taken to infer priority payments.

This Court adopted the view of Starke J in the case of *Federal Commissioner of Taxation v. Official Liquidator of E. O. Farley Ltd*. [1940] 63 CLR 278 where it states that the setting aside of money sufficient to provide for taxation is only an administrative function. It does not confer priority rights over other claims.

In *Federal Commissioner of Taxation v. Official Liquidator of E. O. Farley Ltd.*, the words used in the Australian statutes are rather similar to s. 70 of our Sales Tax Act and it is clearly decided by the High Court of Australia that setting aside of money sufficient to provide for taxation does not confer priority rights of payment. Such privileges of priority payment must be in clear and unequivocal words from Parliament and not by mere implication.

In fact s. 23 of the Sales Tax Act refers that sales tax should be recovered by way of "a civil debt".

Section 23(1) states as follows:

> Without prejudice to any other remedy, and sales tax due and payable and any penalty accruing under this Act, may be recovered by the Minister as a civil debt" due to the Government.

As sales tax is a civil debt as defined by s. 23 of Sales Tax Act then s. 10 of the Government Proceedings Act applies. Section 10 gives this debt a preferential treatment for payment over:

> all debts or claims of every kind which shall subsequent to such date, have been contracted or incurred by or become due from such person to any other person whomsoever "except" any right vested in any person by virtue of a mortgage or charge of immovable property duly registered in the manner provided by law for the registration of such mortgage or charge.

Therefore in this case there are two questions that need to be determined.

Firstly, the date of the occurrence of the sales tax as compared with the date when the debt was due to debenture holders.

Secondly, is the debenture holders' right vested in them by virtue of a mortgage or charge of immovable property duly registered in the manner provided by law?

From the affidavits before this Court, the sales tax in this case were incurred before the appointment of the Receivers.

When were the debts due by Setama to the debenture holders?

Section 5.07 of the debenture states as follows:

> Section 5.07 Prepayment.
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> The Borrower shall have the right upon payment of all accrued interest up to the date of prepayment of the loan as hereinafter provided and payment of a premium calculated at the percentage specified in the Third Schedule hereto and upon not less than ninety (90) days notice in writing to MIDF to repay in advance of maturity:
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> (a) all the principal amount of the loan at the time outstanding; or
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> (b) any one or more of the instalments of the principal amount of the loan maturing at the respective dates specified in the second schedule hereto, Provided That on the date of such repayment there shall not be outstanding any portion or instalment so prepaid.

Deducting from the above, the Receivers must have been appointed due to a default of payment by Setama. Such being the case, the debt due to the debenture holders can be taken as the date of appointment of the Receivers. Under such circumstances this debt was due after the sales tax was incurred.

As for the second question, this Court finds that the fixed charge in this case is not related to "immovable property".

Section 6.01(a) of the debenture clearly states as follows:

> by way of a first fixed charge over all the borrowers plant, equipment and machinery set out in the fourth schedule hereto including all plant, equipment and machinery hereafter acquired together with accessories and parts pertaining thereto.

The assets secured are in fact movable properties. Under such circumstances it does not qualify under the exception of s. 10(2) of the Government Proceedings Act.

In view of the aforesaid this Court finds that sales tax being a debt owed to the Government ranks in priority over fixed charge of debenture holders in this case.

This Court therefore orders:

(1) that prayer 1 of the originating summons be dismissed,

(2) that sales tax due to the Government be paid in priority to debenture holders of the first fixed charge in this case and

(3) no order as to costs of this application.

Also found at [1991] 1 CLJ 495